MEMORANDUM FOR
THE CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM

Washington Monthly Report

In the wake of last year's partisan trainwreck over the Federal budget that led to a single omnibus spending bill, the GOP Leadership in Congress vowed a return to the regular order in which the 13 individual appropriations measures would be prepared under the regular procedures and sent to the President for signature. Large looming federal budget surpluses as far as the eye could see seemed to ease the task.

However, the partisan trains are once again speeding towards each other, and the sound of twisting metal should be heard in the late summer. Last year's tight budget spending caps -- which contributed to last year's budget debacle -- have ratcheted down even lower, requiring deep cuts in existing programs and making some appropriations bills impossible to enact. The expectation now is that many of these bills will be sitting unenacted as the September 30 end of the fiscal year approaches.

Complicating matters on the spending side, the House and Senate Republican Leadership wants to enact massive tax cuts on the order of almost $800 billion over 10 years -- the largest tax cut in 18 years -- to try to restore the distinctive message of the Republican party. This tax cut would absorb the bulk of the non-Social Security surplus projected over the next 10 years, leaving little cushion for additional spending to ameliorate the budget cap problem. Indeed, the large projected surpluses used to fund the GOP tax cut assume that the tight budget caps will stay in place and continue ratcheting down in future years. Democrats have countered that the long-term solvency of Medicare and Social Security should be preserved first, before having a large tax cut. The President has announced that he will veto a tax cut of the scope being pursued by Congressional Republicans.

All of this has led to the expectation that a "global" budget negotiation between the Administration and the Congressional Leadership will be necessary to keep the federal government running for the first year of the 21st Century. In exchange for flexibility on the tax cuts sought by Congressional Republicans, the Administration and Congressional Democrats are likely to press for additional spending and preservation of the long-term solvency of Medicare as well as a new Medicare prescription drug benefit. The politically volatile issue of Social Security solvency could be staved off by setting the Social Security trust fund surplus aside under the so-called “lock box’ concept to assure future solvency for some period, while leaving the difficult issue of an actual substantive reform plan for a future day.

Since July will be taken up with tax cut legislation and Congress traditionally blows town for the month of August, this leaves September and early October to tackle and resolve these thorny budget issues.

Mandatory Social Security

The House Ways and Means and Senate Finance Committees have spent this month drafting their respective tax cut packages, leaving little time to focus on Social Security reform. Throughout the House consideration of tax cut legislation, Democrats have kept to their mantra of “Save Social Security and Medicare First.” No effort has been made to bridge the partisan divide on this politically sensitive issue of Social Security reform, and if anything the harsh partisan rhetoric has pushed the two sides father apart.

There seems to be little likelihood that any serious attention would be paid to actual substantive Social Security reform until Congress returns in September from its summer recess, at the earliest. At that time, it is possible that substantive Social Security reform could be taken up as part of the expected “global” budget summit. However, the more likely scenario is that some dollar amount of the expected surplus will be put aside for Social Security, with details to be dealt with in the future.

What does this all mean for mandatory Social Security? We have been encouraged thus far that with the exception of Senator Daniel Patrick Moynihan’s (D-N.Y.) proposal, none of the various other major Social Security reform plans proffered thus far has included mandatory Social Security. Clearly, the effort over the last year by the public plan community to activate its grassroots -- as STRS has so effectively done with the California Congressional delegation -- has had a significant impact, as have the development of arguments about the harsh cost impact on existing State and local government spending programs across-the-board. No longer is mandatory Social Security seen as some sort of “no brainer” or “free money” in which the non-Social Security States are swept into Social Security as though their exclusion was the product of some “rounding error” previously overlooked.

For now, we will be forced to wait-and-watch, to see whether Congress and the Administration actually turn to the substantive details of Social Security reform. Key factors in whether mandatory Social Security reemerges as a possible funding option will be whether Congress and the Administration seek to achieve solvency for the full 75-year actuarial period and how much of the non-Social Security surplus is set aside (along with the surpluses arising in the Social Security trust fund) to fund the solvency effort. In the meantime, STRS and the employee groups should keep up the steady stream of complaints to the California Congressional delegation about the harsh adverse impact that mandatory Social Security would have on State and local government programs.

Appropriation for Elk Hills Compensation

With the ratcheting down of the federal budget caps wreaking havoc with this year's Congressional appropriations process, we have faced a steep uphill climb on the $36 million appropriation necessary for the next annual installment of Elk Hills compensation due for FY 2000.

We are pleased to report that with a lot of hard work dating back to the gathering of the 52 signatures of the entire California Congressional delegation on a letter to the House Appropriations Committee and Subcommittee Chairmen in support of Elk Hills compensation, the Interior Appropriations measure approved by the full House of Representatives on July 14 does contain the necessary funding for the $36 million Elk Hills compensation payment.

Rep. Bill Thomas (R-Bakersfield) continues to be the tireless champion of our cause, and we received the unanimous support of the six Californians on House Appropriations: Reps. Jerry Lewis (R-Redlands), Ron Packard (R-San Clemente), Duke Cunningham (R-Escondido), Julian Dixon (D-Los Angeles), Nancy Pelosi (D-San Francisco), Lucille Roybal-Allard (D-Los Angeles), and Sam Farr (D-Monterey).

We will be coordinating with Rep. Thomas and Sen. Feinstein to develop strategy for the House-Senate Conference to resolve the differences between the House Interior measure which contains Elk Hills funding and the Senate measure which left Elk Hills funding out to have a bargaining chip for Conference with the House and with the Administration. The Conference is expected to be held sometime in September.

Pension Liberalization Legislation

Both the House Ways and Means Committee tax bill and the Senate Finance Committee tax bill contain the provisions described in previous Monthly Reports that would enhance pension portability among State and local government plans, as well as a broad-ranging series of other liberalizing changes to benefit limits. May of these were drawn from the comprehensive Portman-Cardin legislation (H.R. 1102).

With the state of the tax bills very much in flux, we will review the provisions in greater detail once a final legislative package has been developed.

Possible Amendment to Limit Protection of Pension Plan Interest Where a Participant Goes Bankrupt

As we first reported last month, Senator Charles Grassley (R-Iowa) is continuing to consider an amendment to the bankruptcy reform legislation (S. 625) pending in the Senate under which the amendment would cap at $250,000 the value of a participant's pension plan interest that would be exempt from creditors when a participant files for bankruptcy.

All of the various national groups representing State and local plans, employers, and employees have prepared a joint letter to Sen. Grassley strongly urging him to refrain from offering such an amendment. The private sector pension groups also are vociferously opposing such an amendment. (As well as being a poor idea, the amendment is poorly drafted by defining "pension plan" as an ERISA-covered plan, thereby apparently inadvertently omitting State and local government plans, which are exempt from ERISA).

John S. Stanton

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